

BILL # SB 1244

TITLE: insurance premium tax rate

SPONSOR: Gorman

STATUS: As Introduced

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FISCAL ANALYSIS

Description

The bill would reduce the insurance premium tax for life insurers and property and casualty insurers. The tax rate for these types of insurers is currently 2% of their net premium income. Starting in CY 2008, the bill would reduce the tax rate by 0.1% each year until the rate reaches a level of 1.5% in CY 2012 and beyond.

Estimated Impact

Based on estimated growth rates in life insurance and property and casualty insurance premiums provided by the Department of Insurance (DOI), the bill would reduce General Fund revenues by \$(12,214,000) in FY 2009, which would grow to \$(54,553,100) once the bill is fully implemented in FY 2013.

DOI has a similar estimate of the General Fund impact.

Some of the revenue loss to the General Fund may be offset if the reduced tax rate encourages more insurance companies to relocate to Arizona. This analysis does not attempt to quantify the magnitude of this impact. Given that the tax rate reduction is not fully implemented until CY 2012, any “dynamic” impact associated with additional insurance activity may take several years to occur.

Analysis

Insurance premium tax is imposed on net insurance premiums received by insurance companies for risks that exist within the state. The tax is imposed on different types of insurance premiums, but the bill would only reduce the tax for life premiums and property and casualty premiums. The insurance premium tax for life insurers and property and casualty insurers is 2% of their net premium income. Net premium income is the total amount received from premiums less cancellations, returned premiums, policy dividends, refund reductions, savings coupons, and similar amounts or credits to policyholders within the state. Revenues generated from the tax on life premiums and property and casualty premiums are deposited into the state’s General Fund.

Starting in CY 2008, the bill would reduce the insurance premium tax rate for life insurers and property and casualty insurers from the current 2% rate to a rate of 1.5% over the next 5 years.

In FY 2006 the General Fund received \$373,682,400 in total premium tax collections. Based on an analysis of the insurance market components, along with economic and demographic factors, DOI expects collections to grow at an average annual rate of 4.5%. Under existing law, this would amount to \$434,991,300 in FY 2009. By reducing the tax rate to 1.9% for life insurance and property and casualty insurance premiums in CY 2008, General Fund revenues would instead be estimated at \$422,777,300 in FY 2009, a reduction of \$(12,214,000). Since the bill would become effective January 1, 2008, collections would only be impacted in the second half of FY 2009. Once the bill is fully implemented in FY 2013, with a tax rate of 1.5%, collections would be reduced by \$(54,553,100).

These estimates are based on a static model and do not incorporate “dynamic” estimates. Dynamic forecasting goes beyond the static approach and attempts to predict changes in the economy brought about by changes in tax policy. The bill could result in more insurance policies written in Arizona due to the lower rate, and could encourage insurance companies to “re-domesticate” to Arizona or to form in the state. Existing law does not require an insurance company to have a physical presence in the state in order to be considered an Arizona-based insurer. However, as part of the process of forming or domesticating, the bill may ultimately result in more insurance companies with a physical presence in the state.

Insurance premium tax also includes “retaliatory” taxes. This type of tax is paid by companies that are formed in one state, but sell insurance in another state. These companies are obligated to pay retaliatory taxes if taxes paid in the home state would be greater than taxes levied in the other state. As of result of these retaliatory taxes, the bill could also offer a competitive advantage to Arizona-based insurance companies that sell insurance in other states. Since the tax rate in Arizona would be lowered under the bill, Arizona-based insurers that sell insurance in other states with lower tax rates than Arizona would owe less in retaliatory taxes to those other states.

Arizona’s current life insurance premium tax rate is greater than the rate imposed by 15 states. The current property and casualty insurance premium tax rate is greater than the rate imposed by 13 states.

In February 2005 Ernst & Young conducted a study on the effects of a proposal to reduce New Hampshire’s insurance premium tax rate for life insurers and property and casualty insurers from 2% to 1%. The study projected that the rate reduction would increase New Hampshire’s competitiveness relative to competitor states and would increase employment in terms of attracting new start-up and re-domesticating insurance companies. The study estimated that the generation of jobs would offset 64% of the revenue loss as a result of the lowered rate. The study also cited Ohio, which lowered its premium tax rate from 2.5% to 1.4% during the time period 1998 to 2003. Compared with other states, Ohio had the most net re-domestications of property and casualty insurers during that time period.

Local Government Impact

None

2/14/07